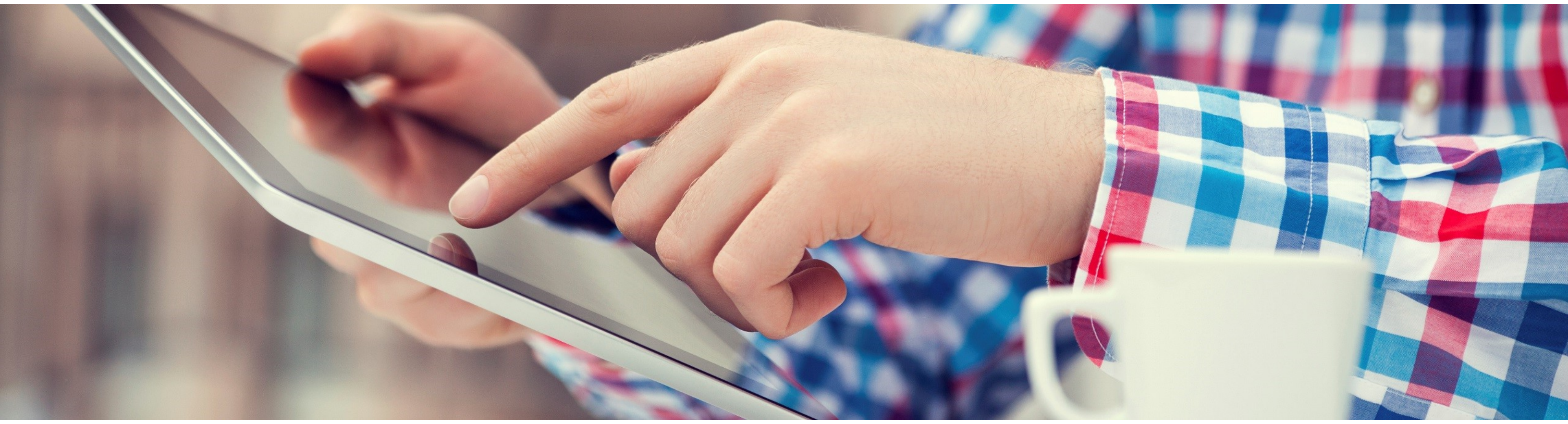
Partial Exchanges

Defer Some Capital Gain Taxes and Recognize Some Gain



Although a 1031 exchange provides the opportunity for taxpayers to potentially defer all of their capital gain tax liability, some taxpayers make the decision to perform a partially deferred exchange for a variety of different reasons.

WHAT IS A PARTIAL EXCHANGE?

In a partial exchange, the taxpayer decides to defer some capital gain taxes and also pay potentially recognized gain on either 1) cash proceeds received; or, 2) a reduction on the taxpayer's replacement property mortgage as compared to the relinquished property mortgage. Both of these events result in the receipt of "boot" which refers to any property received in an exchange that is not considered like-kind real property [Cash boot refers to the receipt of cash. Mortgage boot is a term describing a taxpayer's reduction in mortgage liabilities on the replacement property purchase.]

WHEN CAN CASH PROCEEDS BE RECEIVED?

Cash proceeds can be received as follows:

1. When a taxpayer specifically instructs the closing officer to disburse a fixed dollar amount of the sale proceeds to them directly from the relinquished property closing and having the remaining amount transferred to the qualified intermediary to be included in the 1031 exchange.

- or -

2. After all identified property has been purchased or after the end of the exchange period (generally 180 days) if there are replacement properties which have been properly identified by the taxpayer but not purchased pursuant to the 1031 exchange.

WHAT ARE THE REQUIREMENTS FOR FULL TAX DEFERRAL IN A 1031 EXCHANGE?

If a taxpayer intends to perform a 1031 exchange that is fully tax deferred instead of partially deferred, they should meet two specific requirements:

1. Reinvest the entire net equity (net proceeds) in one or more replacement properties;

- and -

2. Acquire one or more replacement properties with the same or a greater amount of debt. [One exception to the second requirement is that a taxpayer can offset a reduction in replacement property debt by adding cash to the replacement property purchase.]

WHEN NOT TO DO A 1031 EXCHANGE

Generally, if the taxable boot is greater than the amount of the capital gain, it may not be feasible to do a 1031 exchange. Every taxpayer should review their specific 1031 exchange situation with a tax and/or legal advisors before closing on the sale of the relinquished property.

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